(15)

No. 95-860

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

BARBARA SMILEY,

Petitioner,

v.

CITIBANK (SOUTH DAKOTA), N.A.,

Respondent.

ON WRIT OF CERTIORARI TO THE CALIFORNIA SUPREME COURT

BRIEF OF THE NEW YORK CLEARING HOUSE ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENT

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38 pp

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Legislative Materials

Administrative Materials

Other Authorities

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Pursuant to Rule 37.3 of this Court, The New York Clearing House Association (the "Clearing House") respectfully submits this brief as *amicus curiae* in support of Respondent Citibank (South Dakota), N.A. ("Citibank") with the consent of all parties.

Interest of *Amicus Curiae*

The Clearing House is an association of eleven leading commercial banks in the City of New York, including an affiliate of Citibank.[1] The Clearing House regularly appears as *amicus curiae* in cases raising important issues relating to banking, and its members have a common and vital interest

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[1] The members of the Clearing House are The Bank of New York, The Chase Manhattan Bank, N.A., Citibank, N.A., Chemical Bank, Morgan Guaranty Trust Company of New York, Bankers Trust Company, Marine Midland Bank, United States Trust Company of New York, NatWest Bank National Association, European American Bank and Republic National Bank of New York.

in the consistent and uniform application of the banking laws of this country.

The issue raised in this appeal concerns state efforts to regulate credit card late charges assessed by national banks. Four members of the Clearing House are national banks governed by the National Bank Act (the "Act") and supervised by the Office of the Comptroller of the Currency ("OCC"), a bureau within the Department of the Treasury. 12 U.S.C. §§ 21 *et seq.*[2] Under Section 30 of the Act, codified as 12 U.S.C. § 85 ("Section 85"), a national bank is permitted to charge "interest" to its customers — wherever located — at the highest rates authorized by the bank's home state. The other seven members of the Clearing House are state-chartered banks governed by a statutory provision modeled after Section 85 — Section 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980, 12 U.S.C. § 1831d (1994) — that grants state banks the same authority as Section 85 grants national banks.

The sole issue in this case is whether Section 85 should be interpreted — contrary to the consistent position of the OCC — to exclude from the definition of "interest" the late payment charges for loans that are typically included in credit card agreements. The Clearing House's member banks have relied on the OCC's interpretations in structuring their credit relationships with customers for years, and would face a substantial burden if forced to vary the financial terms of their credit card programs to comply with the different late charge regulations imposed, from time to time, by the 50 states. In addition, the banks could no longer offer credit card programs on a uniform national basis.

[2] The OCC was created in 1863 by the National Currency Act, ch. 58, § 1, 12 Stat. 665-66 (1863), and given the power to regulate national banks in both that statute and the National Bank Act, ch. 106, § 1, 13 Stat. 99-100 (1864).

Summary of Argument

The decision below affirmed the consistent interpretation of Section 85 adopted for many years by the OCC — the regulatory agency charged with supervision of national banks — and the courts that "interest" includes late charges. (*See* A 26-28.)[3] This interpretation is consistent with Congress's objective in adopting the Act as a whole and Section 85 in particular.[4]

Congress adopted the Act to establish a strong national banking system which could provide credit across state lines free of state-law impediments. This objective was a product of the Civil War: both because (1) the war created a critical need for a stable and strong national banking system capable of financing the war effort and (2) many fewer opponents of federal fiscal power were in Congress after the Southern states seceded from the Union. Knowing the potential for hostile and inconsistent state regulation, Congress adopted a uniform regulatory scheme governed exclusively by federal law.[5]

[3] Citations to the decision below, in the form "A __," are to the appendix to the petition for certiorari.

[4] Subsequent to the decision below, the OCC, in accordance with the procedures of the Administrative Procedure Act, adopted a regulation reaffirming its prior interpretations of Section 85. *See* 61 Fed. Reg. 4849, 4869 (1996) (to be effective on April 1, 1996 and codified at 12 C.F.R. § 7.4001).

[5] Although Section 85 adopts the most favorable rate allowed to *any lender* by a national bank's home state as the highest rate the bank may charge, a national bank's lending charges are governed solely by federal law, *i.e.*, Section 85 does not permit any concurrent state regulation of national banks' lending charges nor does it involve a delegation of federal authority over national banks to the states. Thus, a national bank's home state may *not*, by statute or otherwise, impose a lending rate on national banks that is lower than the rate prescribed by Section 85 nor provide *any* remedies for breaching either Section 85 or a state-imposed lending limit

(continued...)

The OCC's definition of interest under Section 85 as including late charges is consistent with the historic use of "interest" to encompass a broad range of loan-related charges. This is apparent in academic materials, dictionaries and judicial opinions from the mid-nineteenth century and before, as well as the established banking practices of the time. Moreover, a federal definition of interest which includes late charges is consistent not only with the prevailing understanding of the word interest at the time of the Act's enactment, but with Congress's intent to provide a strong banking system of national scope.

ARGUMENT

Section 85 authorizes national banks to charge "interest at the rate allowed by the laws of the State . . . where the bank is located." 12 U.S.C. § 85. There is no dispute that this provision authorizes a national bank to impose periodic percentage interest charges on a customer's outstanding credit card balance to the extent permitted by the national bank's home state. The question in this case is whether delinquency charges — that is, the amount charged to a borrower because the borrower fails to repay amounts due on time — constitute "interest" governed by this provision.

The briefs of the parties examine at length the authorities interpreting Section 85. They show that Section 85 has been repeatedly applied by the courts, and by the OCC, to all of the charges received by a bank as compensation for lending, however denominated. Moreover, recent judicial deter-

[5](...continued)
— the exclusive remedies for overcharging by a national bank are provided by 12 U.S.C. § 86 ("Section 86"). *Farmers' & Mechanics' Nat'l Bank* v. *Dearing*, 91 U.S. 29 (1875). *A fortiori*, Section 85 does not permit concurrent regulation by the home state of a national bank's borrower.

minations have also held that Section 85 applies to credit card late fees.[6]

The historical analysis which is the focus of this brief demonstrates that these decisions are fully consistent both with Congress's goals in passing the Act and with the use of the term "interest" at the time of the Act's adoption.

I. The National Bank Act Was Enacted by Congress To Provide for a Uniform Currency and an Interstate Lending System Administered Through a Strong National Banking System.

Congress passed the Act in 1864, in the midst of the Civil War, in order to provide for a strong national banking system. Such a system required federally chartered banks that could provide a uniform currency and participate unfettered in interstate lending. At the time, Congress knew from experience that powerful political forces existed at the state level that would seek to protect local state-chartered banks and to undermine the effectiveness of out-of-state federally chartered banks. The Act was designed, in part, to prevent this frustration of Congressional purpose by the states. Section 85 was specifically aimed at (1) protecting national banks from discrimination in favor of state-chartered banks and (2) state interference with national banks' ability to engage in interstate commerce through balkanized regulation of lending charges.

[6] *See, e.g.*, *Greenwood Trust Co.* v. *Massachusetts*, 971 F.2d 818 (1st Cir. 1992), *cert. denied*, 506 U.S. 1052 (1993); *Copeland* v. *MBNA America Bank, N.A.*, 907 P.2d 87 (Colo. 1995). The only appellate courts to have reached the opposite conclusion are the New Jersey Supreme Court (by a 4-3 division), and the Pennsylvania Superior Court (by a 6-3 vote). *See Sherman* v. *Citibank (South Dakota), N.A.*, 668 A.2d 1036 (N.J. 1995); *Mazaika* v. *Bank One, Columbus, N.A.*, 653 A.2d 640 (Pa. Super. Ct. 1994), *appeal granted*, 659 A.2d 557 (Pa. 1995); *see also Gadon* v. *Chase Manhattan Bank, (USA)*, 653 A.2d 697 (Pa. Super. Ct.) (following *Mazaika*), *appeal granted*, 659 A.2d 557 (Pa. 1995).

A. The Civil War Provided Both the Need and Political Opportunity for a National Banking System.

Prior to 1864, the nation's banking system was a "decentralized, unstable structure of state banks" with frequent failures and under which there was no uniform federal currency.[7] In the absence of federal involvement, banking was a function of disparate state regulation.[8] The economy was hampered not only by an often loose state chartering and regulatory approach, which resulted in frequent bank failures, but also by the absence of a national form of paper currency. The ability of businesses to engage in interstate commerce in an efficient manner was undermined by a haphazard system of privately issued bank notes of uncertain and varying value, especially when transactions involving those notes occurred in locations remote from the issuing bank.[9]

Congress had earlier established the First and Second Banks of the United States to address these problems.[10]

[7] JAMES M. MCPHERSON, BATTLE CRY OF FREEDOM 594 (1988).

[8] *See* David M. Gische, *The New York City Banks and the Development of the National Banking System, 1860-1870*, 23 AM. J. LEGAL HIST. 21, 24-25 (1979).

[9] *See id.* Representative Samuel Hooper, chief sponsor of the Act in the House of Representatives, decried that a nation "which leaves the power to regulate its currency to the legislation of thirty-four different states abandons one of the most essential attributes of its sovereignty." BRAY HAMMOND, SOVEREIGNTY AND AN EMPTY PURSE 314 (1970) [hereinafter HAMMOND, SOVEREIGNTY] (quoting from debates on the National Currency Act of 1863).

[10] *See Treasury Report on a National Bank* (Dec. 13, 1790), *in* 1 DOCUMENTARY HISTORY OF BANKING AND CURRENCY IN THE UNITED STATES 230, 233-34 (Herman E. Kross ed. 1969) [hereinafter KROSS]; *Opinion of Alexander Hamilton, On the Constitutionality of a National* (continued...)

Those Banks were short-lived, however, falling victim to the ongoing political struggle between advocates of a strong central government (primarily the industrial and commercial interests in the North) and advocates of "states' rights" (primarily in the South and West). *See* SISTER M. GRACE MADELEINE, MONETARY AND BANKING THEORIES OF JACKSONIAN DEMOCRACY 8-9, 11 (1943) [hereinafter BANKING THEORIES].

The First Bank of the United States was established by Alexander Hamilton and the Federalists in 1791, over the strong opposition of Thomas Jefferson, James Madison, and other Jeffersonians generally fearful of a strong national government. When the Jeffersonians gained power in 1801, the Bank again became a political issue, with the states opposing the Bank's domination of credit throughout the country. Although the Bank had proved to be an "unqualified success," President Madison and his supporters in Congress permitted the Bank's charter to expire in 1811. *See id.* at 6-12.

Shortly after the First Bank's demise, financial chaos resulted from the rapid multiplication of small independent state banks. *Id.* at 12-15. This led Congress to establish the Second Bank of the United States in 1816. *See* Act of April 10, 1816, ch. 44, 3 Stat. 266. But the aggressive expansion of the Second Bank caused many states — particularly those in the South and West — to enact legislation "designed to cripple the activities of the 'Chestnut Street Monster' and to destroy its power within their jurisdictions." BANKING THEORIES, *supra*, at 21. Some states enacted constitutional amendments to prohibit the Second Bank from operating within their jurisdictions; other states tried to impose

[10](...continued)
Bank (Feb. 23, 1791), *in* LEGISLATIVE AND DOCUMENTARY HISTORY OF THE BANK OF THE UNITED STATES 95, 108 (M. St. Clair Clarke & D.A. Hall ed. 1967) (1832); *Recommendations from Secretary of the Treasury Alexander Dallas on a National Bank* (Oct. 17, 1814), *in* KROSS, *supra*, at 396-97.

prohibitive taxes. *Id.* at 21-22. A Maryland statute imposing a heavy stamp tax on all notes issued by banks incorporated outside the state led to this Court's decision in *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819), declaring such state taxes unconstitutional.[11]

Opposition to the Second Bank culminated in President Jackson's veto of the Bank's recharter in 1832. The public "war" on the Bank was born in large part from the "undying hostility of the states"[12] and was in reality a fierce political debate over who would control banking. Jackson sided with those in favor of "states' rights" and, once again, a federal banking system was destroyed.

The problems created by a state-governed banking system became critical during the Civil War. As the debates surrounding the Act demonstrate, financial stability was imperative in order to enable the federal government to raise badly needed funds for the Union's war effort and otherwise to support the economy.[13]

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[11] *See also Osborn* v. *Bank of United States*, 22 U.S. (9 Wheat.) 738 (1824). This Court's decisions in *M'Culloch* and *Osborn* spawned intense opposition, particularly in the South and West. *See* BANKING THEORIES, *supra*, at 23-27.

[12] *See* RALPH C.H. CATTERALL, THE SECOND BANK OF THE UNITED STATES 164 (1903). "Nowhere were the centralizing tendencies of the Democratic program perceived more astutely than in the South, which was always vigilant with respect to states' rights." LARRY SCHWEIKART, BANKING IN THE AMERICAN SOUTH FROM THE AGE OF JACKSON TO RECONSTRUCTION 16 (1987).

[13] *See Veazie Bank* v. *Fenno*, 75 U.S. (8 Wall.) 533, 536-39 (1869); *see also* CONG. GLOBE, 38th Cong., 1st Sess. 2132 (1864) ("We are in the very straining point. If we pass this point, we go through. If we fail financially now, we fail altogether.") (remarks of Sen. Chandler); CONG. GLOBE, 38th Cong., 1st Sess. 1257 (1864) ("The loan bill, including the issue of legal-tender notes, the national bank act, and the tax law were recommended by the Secretary of the Treasury as the three measures to be relied upon to carry the nation through the financial difficulties of this

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Congress also recognized that the banking system in the South would need extensive repair after the war. The war had drained finances in the South even more than in the North, leaving many Southern states with no surviving banks at all. Any chance of the South's recovery after the war would necessarily depend on the inflow of capital from the money centers of the North.[14]

To solve these pressing problems, Congress chose to establish a uniform national currency; this in turn required a strong national banking system. As President Lincoln explained, there was "no other mode by which 'the great advantages of a safe and uniform currency' could be achieved so promisingly and unobjectionably as by 'the organization of banking associations under a general act of Congress.'"[15] With many of the most ardent supporters of states' rights absent from Congress as a result of the secession of the

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[13](...continued)
war.") (remarks of Rep. Hooper); *id.* at 1256 ("I frankly confess that I look upon the system of State banks as having outlived its usefulness, as being unequal to the exigencies of the present time, with the demands which this war is making on the resources of the country and on its financial and monetary systems.") (remarks of Rep. Hooper).

[14] *See* CONG. GLOBE, 37th Cong., 3d Sess. 841 (1863) (speaking in favor of the National Currency Act, the precursor to the Act, Senator Sherman asserted: "We know very well that after this war is over . . .; that when the rebellion is subdued, the condition of society in Southern states will be disturbed . . . ."); SCHWEIKART, *supra*, at 309-11. After the war, circulation of bank notes was disproportionately high in the North and disproportionately low in the South. Gische, *supra*, at 62.

[15] HAMMOND, SOVEREIGNTY, *supra*, at 290. In 1887, this Court explained that "[t]he object of the [Act] was to establish a system of national banking institutions, in order to provide a uniform and secure currency for the people, and to facilitate the operations of the treasury of the United States." *Mercantile Nat'l Bank* v. *New York*, 121 U.S. 138, 154 (1887).

Southern states, a national banking system under federal control was now politically feasible.[16]

B. In Enacting the National Bank Act, Congress Recognized and Sought To Neutralize State Hostility to National Banks.

The history of state hostility towards the First and Second Banks of the United States provided Congress with ample experience as to the likely reaction of many states to federally chartered banks. Congress understandably expected states to attempt to enact burdensome and discriminatory legislation against banks chartered under the new federal system and to attempt to impose restrictions on out-of-state banks. As Representative Davis stated:

> But whether right or wrong, I am willing to do anything that may be thought best in favor of strengthening this [national system] and the banks that are to be organized under it in the impending conflict with the State institutions.[17]

This Court has consistently recognized this Congressional concern and interpreted the Act in a manner aimed at limiting the ability of the states to regulate national banks in order to ensure that national banks could compete effectively with state banks and on a national basis. *See, e.g.*, *Tiffany* v.

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[16] *See* 1 A HISTORY OF BANKING IN ALL THE LEADING NATIONS 464 (William G. Sumner ed. 1971) (1896) ("It is a great point which must be put to the credit of the civil war that it brought about what was otherwise a political impossibility": a national banking system).

[17] CONG. GLOBE, 38th Cong., 1st Sess. 1400 (1864) (remarks of Rep. Davis). *See also id.* at 1894 ("Of course the new system must begin in rivalry with the State banks, which in many cases will be hostile.") (remarks of Sen. Sumner); *id.* at 1393 ("to carry out that object [to make this a great national system] it will not do to place it in the power of the States, otherwise you place it in the power of any State which may be opposed to the system to cripple and destroy it") (remarks of Rep. Washburn).

National Bank, 85 U.S. (18 Wall.) 409, 412-13 (1874) ("it was intended to give [national banks] at least equal advantages in" competition with state banks); *Dearing*, 91 U.S. at 33-35; *Marquette Nat'l Bank* v. *First of Omaha Serv. Corp.*, 439 U.S. 299, 313-18 (1978).

To protect the newly formed national banks from potentially destructive state legislation, the Act provided that the regulation of national banks was to be a matter of federal law and enacted a comprehensive — and exclusive — regulatory scheme. One aspect of this scheme was Section 85, in which Congress specified that a national bank was authorized under *federal* law to charge borrowers — wherever located — the highest rate allowed by the national bank's home state, even if that rate was higher than the rate which could be charged by state banks.[18] Moreover, Congress provided that any challenge to a national bank's lending charges could be brought only under federal law. 12 U.S.C. § 86; *Dearing*, 91 U.S. at 32-36.

Initially, Congress considered establishing a uniform usury rate for national banks (and it did so where a state or territory provided no rate). *See Daggs* v. *Phoenix Nat'l Bank*, 177 U.S. 549 (1900). But Congress ultimately rejected that idea, and instead decided to place national banks "on precisely the same footing [as lenders] doing business in the [bank's home] State by its laws."[19] Thus, lending rates

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[18] *Tiffany*, 85 U.S. (18 Wall.) at 411-13. In this respect, Section 85 is consistent with other provisions of the Act which apply federal definitions to the terms used in the Act even in provisions incorporating state law. *See* 12 U.S.C. §§ 36 (branching), 92a (trust powers); *First Nat'l Bank* v. *Dickinson*, 396 U.S. 122, 131-34 (1969) (term "branch" in 12 U.S.C. § 36 is defined by federal law).

[19] CONG. GLOBE, 38th Cong., 1st Sess. 2126 (1864) (remarks of Sen. Sherman). Congress rejected an amendment that would have allowed state legislatures discretion to *reduce* the amount of "interest" a national bank could charge below that which a state bank could charge. As (continued...)

were immune, as a practical matter, from state discrimination because a state could limit a national bank's lending rates only by imposing identical restrictions on *all* local lenders. Section 85 was structured to advance Congress's goal of protecting national banks from "the hazard of unfriendly legislation by the States." *Tiffany*, 85 U.S. (18 Wall.) at 413.

Congress's concern that national banks be protected from "unfriendly legislation" was no doubt increased by the possibility that the Southern states might soon be readmitted to the Union, either by peaceful or military means. At their national convention in August 1864, the Democrats nominated General McClellan for President on a "peace" platform, which demanded restoration of the "Federal Union" by calling for "an ultimate convention of the states" without mention of the divisive issue of slavery. *See* McPherson, *supra*, at 771-72.[20] At the same time, Congress expected that even if "peace" were not achieved in such fashion, the North would eventually prevail in the war and readmit the Southern states to the Union on its terms.[21]

Given that Congress anticipated that the Southern states — long home to the most zealous advocates of "states' rights" and foes of federally chartered banks — would be

[19](...continued)
Representative Pike stated: "[W]ould it not enable the Legislature of a State to kill off the national banks of that State?" *Id.* at 1375 (remarks of Rep. Pike).

[20] There was considerable speculation at the time that McClellan might actually defeat Lincoln in the fall elections. Indeed, for a period of time Lincoln himself expected McClellan to win. *See id.* at 771.

[21] As of June 1864, military or provisional civil governments were in place in occupied Arkansas, occupied Louisiana, occupied North Carolina (coastal region), occupied Tennessee, and occupied Texas (coastal region). *See* Roy G. Glashan, American Governors and Gubernatorial Elections, 1775-1978, at 17, 113, 230, 291, 298 (1979).

extremely hostile to the new federal banking associations, protection from hostile state legislation was vital to enabling national banks to engage in business in the South.

A key reason for protecting national banks from hostile state legislation was to create a strong national banking system that could operate effectively in interstate commerce. *See Marquette*, 439 U.S. at 314-15 ("Congress intended to facilitate what Representative Hooper termed a 'national banking system.'") (quoting Cong. Globe, 38th Cong., 1st Sess. 1451 (1864) (remarks of Rep. Hooper)). Reviewing the provisions and legislative history of the Act, the *Marquette* Court concluded that Congress "recognized the interstate nature of American banking." *Id.* at 315-17 (noting the "developed interstate loan market" in 1864).[22]

In fact, the Civil War Congress envisioned that national banks would ultimately *replace* state banks, and in March 1865 (less than one year after the Act was passed) it attempted to tax state banks "out of existence" with a ten percent confiscatory tax on state bank notes. *Tiffany*, 85 U.S. (18 Wall.) at 413; *see* Internal Revenue Act of 1865, ch. 78, § 6, 13 Stat. 469, 484.[23] Although this attempt

[22] *See also* Cong. Globe, 38th Cong., 1st Sess. 2021 (1864) ("[National] banks will, of course, have very extensive loan transactions all over the country. They are organized for that purpose.") (remarks of Sen. Johnson).

[23] Congressional debates show that Congress's purpose in enacting the ten percent tax was to destroy the state banks. *See* Cong. Globe, 38th Cong., 2d Sess. 1139 (1865) ("The national banks were intended to supersede the State banks. Both cannot exist together . . . .") (remarks of Sen. Sherman); *id.* at 1195 ("Many members who were in favor of taxing State banks out of existence could not agree upon the terms. Finally, however, they did agree upon this fifth section. That will, I think, effectually do the work . . . .") (remarks of Sen. Sherman).

ultimately failed,[24] the unmistakably clear intent of the Civil War Congress which enacted the Act was to centralize power over the national economy by means of a strong national banking system and to immunize that banking system from state control. The Act was framed to achieve those ends.

II. By Providing That a National Bank Could Charge "Interest" at the Highest Rate Allowed in Its Home State, Congress Advanced Its Goal of Creating a Strong National Banking System.

Section 85 is a provision specifically designed to carry out Congress's goal of creating a strong national banking system.[25] By its terms, a national bank could charge the highest "interest" allowed any lender by the laws of the state in which the bank was located. By using the broad term "interest" — which applied to a variety of lending charges — Congress substantially advanced its goal of establishing a strong national banking system subject to uniform, non-discriminatory lending restrictions and able to compete effectively in interstate commerce.

A. The Plain Meaning of Interest in 1864 Included All Lending Charges.

To understand the commonly accepted definition of interest in 1864, it is necessary to appreciate the development of that term's usage over time. The concept of interest grew in juxtaposition to the concept of usury, and in both 1864 and today, the two words have significantly different meanings.

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[24] Despite the confiscatory tax on their notes, state banks continued to function as banks of deposit. *See* HAMMOND, SOVEREIGNTY, *supra*, at 347.

[25] *See* CONG. GLOBE, 38th Cong., 1st Sess. 2126 (1864) (remarks of Sen. Sherman); *see supra* note 19.

Under canon law, the practice of usury, defined as the price paid for the *use* of money, was forbidden. SIDNEY HOMER & RICHARD SYLLA, A HISTORY OF INTEREST RATES 73 (3d ed. 1991); (A 18-19 n.7 (quoting 7 OXFORD ENGLISH DICTIONARY 1099-1100 (2d ed. 1989))). Understandably, exceptions arose to this absolute prohibition. Those exceptions became known as "*interesse*" in Roman Law, which was derived from the "Latin verb *intereo* meaning to be lost." HOMER & SYLLA, *supra*, at 73.

The "*interesse*" exceptions to usury were justified as "compensation due to a creditor because of a loss which he had incurred through lending," *id.*, *i.e.*, a charge not for the *use* of money but for the *loss of use* of money. Such losses occurred if either the money could have been used profitably had it not been loaned or the debtor did not repay the loan at the agreed date, in which case a "penalty for delay might be charged." *Id.* at 73-74; *accord Library of Congress* v. *Shaw*, 478 U.S. 310, 315 n.2 (1986) (The "institution of interest originated under Roman law as *a penalty due from a debtor who delayed or defaulted in repayment of a loan*.") (emphasis supplied); (A 18-19 n.7).

By the time the Act was passed, "interest was divided into two great and well defined classes, the first being that of contractual interest, and the second interest allowed as damages" for the detention of a debt. SIDNEY PERLEY, PRINCIPLES OF THE LAW OF INTEREST 5 (Boston, George B. Reed 1893); *accord* EDWARD CARROLL, JR., PRINCIPLES AND PRACTICE OF FINANCE 35 (New York, G.P. Putnam's Sons 1895) ("[i]nterest is charged not only on loans but on debts overdue"). Dictionaries of the era confirm this ordinary usage. *See, e.g.*, 2 T. CUNNINGHAM, A NEW AND COMPLETE LAW DICTIONARY (London 1765) (defining "interest of money" and noting that "[i]nterest is recovered by way of damages, where damages are recovered *ratione detentionis debiti*"); 1 JOHN BOUVIER, A LAW DICTIONARY 733 (Philadelphia, J.B Lippincott & Co., 14th rev. ed. 1877) (defining "interest" as "compensation which is paid by the

borrower of money to the lender for its use, and, generally, by a debtor to his creditor in recompense for his detention of the debt"); (A 18-19 & n.7 (citing three other similar dictionary definitions)).

Similarly, nineteenth century judicial opinions routinely held that "interest" includes "compensation . . . for the use . . . of money, or as damages for its detention." *Brown* v. *Hiatts*, 82 U.S. (15 Wall.) 177, 185 (1872). Indeed, this Court noted in *Shoemaker* v. *United States*, 147 U.S. 282, 321 (1893), "Interest" includes "damages, by reason of the failure of the debtor to pay the principal when due." *Accord United States* v. *North Carolina*, 136 U.S. 211, 216 (1890) ("Interest . . . is allowed by the courts as damages for the detention of money . . ., or of compensation, to which the [lender] is entitled."); *Redfield* v. *Ystalyfera Iron Co.*, 110 U.S. 174, 176 (1884) ("Interest is given on money demands as damages for delay in payment, being just compensation to the plaintiff for a default on the part of his debtor.").[26] Thus, delinquency charges — *i.e.*, additional charges imposed because of late payment — fall squarely within the classic

[26] Many state-court decisions also employed this classic definition in their analyses. *See, e.g.*, *Barnard* v. *Wyllis*, 39 Mass. 291, 294 (1839) (interest "may be given as damages for the detention of a debt after the time when due by the terms of the agreement"); *Griffin* v. *His Creditors*, 6 Rob. (Vir.) 216, 220 (1843) (Virginia statute "declares, that 'the damages due for delay in the performance of an obligation to pay money, are called interest'"); *Hubbard* v. *Callahan*, 42 Conn. 524, 528-30 (1875) ("interest was allowed, in the nature of damages, for the detention of money"); *State* v. *Lott*, 69 Ala. 147, 154-55 (1883) ("Interest, in this State, has long been regarded not as a mere incident of debt . . . for the payment of money, but as compensation for the use, or for the detention of money."); *Sorensen* v. *Central Lumber Co.*, 98 Ill. App. 581, 582 (1901) ("Interest is defined to be, '[t]he compensation which is paid by the borrower of the money to the lender, for its use, and generally, by a debtor to his creditor, in recompense for his detention of the debt.'").

definition of interest, and many nineteenth century cases apply the laws regulating "interest" to such charges.[27]

B. The Narrower Definition of Some Usury Statutes Is Irrelevant in Interpreting Section 85.

In contrast to the traditional definition of interest, the term "usury" referred to "the taking, under contract," of compensation in excess of statutory limits. JAMES A. WEBB, A TREATISE ON THE LAW OF USURY § 1, at 1-2 (St. Louis, The F.H. Thomas Law Book Co. 1899); *see also* 2 JOHN BOUVIER, A LAW DICTIONARY 616 (Philadelphia, T. & J.W. Johnson, 3d ed. 1848) (distinguishing between the terms "usury" and "interest"); A.T. FOLSOM, A SUMMARY OF USURY LAWS AND DECISIONS 1 (1927). There is an obvious relationship between the concepts of usury and interest; if the interest charges are within statutory limits, they are *not* usurious. Nonetheless, in view of the different linguistic and conceptual origins of the two terms, the decisions by some legislative bodies and courts to exclude late charges from the concept of usury does not suggest that late charges are not interest.

[27] *See Greenwood Trust Co.*, 971 F.2d at 825 ("[F]ederal case law has long suggested that, in ordinary usage, interest may encompass late fees and kindred charges."). State courts were in accord. *See, e.g.*, *Wernwag* v. *Mothershead*, 3 Blackf. 401, 402 (Ind. 1834) (five dollars per week late payment charge was permissible "interest at the rate specified in the note from the time it became due"); *Wilkinson (Wilkerson)* v. *Daniels*, 1 Greene 179, 188 (Iowa 1848) (contract providing for three percent late payment charge — raising the loans interest rate from twelve to fifteen percent — "is a contract to pay fifteen per cent. *interest* per annum on a contingency") (emphasis supplied); *Daggett* v. *Pratt*, 15 Mass. 177, 177 (1818) (promissory notes specified "interest at three per cent. per annum, if paid at their maturity; if not, six per cent. interest to be paid"; court held that the six percent charge, which included a three percent late charge, was a proper "interest" charge); *Craig* v. *Pleiss*, 26 Pa. 271, 273 (1856) (flat $25 charge for late payment was "interest" subject to statute limiting permissible rates).

At the outset, the distinction between "usury" and "interest" can be observed from the roots of those terms. The Latin root of usury — *usura* — "means the 'use' of anything, in this case the use of borrowed capital; hence usury was the price paid for the use of money." HOMER & SYLLA, *supra*, at 73. In contrast, as discussed above, "[t]he Latin verb *intereo* means 'to be lost'; [thus] [i]nterest was not profit but loss." *Id.*; (*see* A 18-19 n.7 (discussing similar linguistic analysis in 7 OXFORD ENGLISH DICTIONARY 1099-1100 (2d ed. 1989))).

In Anglo-American jurisprudence, usury has been entirely a matter of statutory law. At common law, there were no limits on charges for the use of money agreed to by the parties. *See, e.g.*, *Sodi, Inc.* v. *Salitan*, 68 So. 2d 882, 885 (Fla. 1953); WEBB, *supra*, § 5, at 3. Many usury statutes, reflecting the origin of the concept of usury, restricted only charges imposed for the use of money and did *not* limit damages for its detention. *See* ROBERT B. COMYN, A TREATISE ON THE LAW OF USURY 72 (1834), *reprinted in* 5 THE LAW LIBRARY (Philadelphia, J.S. Littell, J. Purdon ed. 1834); FRANCIS PLOWDEN, TREATISE UPON THE LAW OF USURY AND ANNUITIES 181 (London 1797).

Moreover, in many cases the decision to exclude late charges from the definition of usury reflected the disfavored status of usury statutes. By the mid-nineteenth century, the moral and religious conceptions underlying usury laws had been largely discredited: many believed that usury statutes were unjust and hindered economic development. *See Lloyd* v. *Scott*, 29 U.S. 205, 224 (1830) ("[t]he act of usury has long since lost that deep moral stain, which was formerly attached to it"); MORTON J. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW: 1780-1860, at 237-45 (1977). State courts reflected this mood by limiting the scope of these

statutes.[28] As a part of this effort, charges or fees which did not directly relate to the use of money were excluded from the calculation of usury.

In light of the distinction between interest and usury, the usury cases on which Petitioner relies, (*see* Brief for Petitioner at 33-39), do not support her contention that, at common law, late fees were not "interest." Instead, these cases merely reflect the fact that many usury statutes restricted only charges imposed on the use of money and were interpreted narrowly. They had nothing to do with the meaning of the term "interest" under the common law or in general usage.[29]

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[28] *See id.* at 244-45 ("it was widely possible by the time of the Civil War to arrange usurious transactions in such a way as to entirely avoid running afoul of the usury laws"); JOHN A. JAMES, MONEY AND CAPITAL MARKETS IN POSTBELLUM AMERICA 82-88 (1978) ("Usury laws were a government-imposed constraint . . ., but we have seen that it was not really a binding one.").

[29] Moreover, despite the restrictive view of some usury statutes, many states included post-maturity charges in determining whether a loan was usurious. *See, e.g.*, *Bang* v. *Windmill Co.*, 96 Tenn. 361, 365 (1896) (note providing for post-maturity charges greater than usury limit held usurious); *Griffin*, 6 Rob. (Vir.) at 220-21 (a provision calling for payment "for the inexecution of an obligation to pay money" is unenforceable because "[a]ny contract or agreement, into whatever shape it may be thrown, which stipulates for more than ten per cent damages, or interest, for the delay to pay money, is illegal"); *Fry* v. *Coleman*, 1 Grant's Cases 445, 447 (Pa. 1857) (agreement to pay flat $100 fee if two notes were not paid within 10 days after maturity is usurious); *see generally* Annotation, *Provision for Interest After Maturity at a Rate in Excess of Legal Rate as Usurious*, 82 A.L.R. 1213, 1218-23 (1933) [hereinafter *Interest After Maturity*] (collecting cases). Some states adopted the test of whether such a charge "was intended as an evasion of the [usury] statute" or "was in fact a device to procure more than lawful interest," while others simply prohibited the charge of greater than the legal maximum after maturity. WEBB, *supra*, § 119, at 135-36, § 121, at 137; *see Interest After Maturity*, *supra*, at 1218-23.

C. Nineteenth Century Banking Practices Confirm That "Interest" Included All Lending Charges.

The banking practices of the nineteenth century confirm that the commonly accepted definition of "interest" was broad. At that time, banks provided credit on a variety of terms and were often compensated in ways other than periodic, time-based percentage rates. Congress understood that banks engaged in these various transactions, and mentioned some explicitly in Section 85. This directly refutes the notion that Congress intended the term "interest" to be as narrow as Petitioner contends.

Some of the more popular banking practices in the mid-nineteenth century included discounts,[30] bills of exchange,[31] loan commissions[32] and compensating balance

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[30] A discount is a transaction whereby a bank advances a customer a sum of money less the discount charged; at maturity, the customer must pay off the entire sum. JAMES, *supra*, at 54.

[31] Bills of exchange were 19th century instruments used both to lend money and transfer that money from one location to another. The transaction was structured as "an order from one person to another living in a different place directing him or her to pay a given amount of money to a third person." *Id.* at 51. The "exchanged" money was often lent by a bank at either a discount or in exchange for periodic loan payments. BRAY HAMMOND, BANKS AND POLITICS IN AMERICA FROM THE REVOLUTION TO THE CIVIL WAR 700 (1957). If the exchange involved two locations where the value of the money was different (if, for example, there was a surplus or shortage of dollars in one of the locations), the bank would charge an "exchange fee" for at least the amount of that difference. *See id.*; JAMES, *supra*, at 53; *infra* pp. 21-22.

[32] Banks often found ways to receive commissions on their loans in addition to a percentage charge. For instance, banks were able to charge commissions for appraising the value of collateral, *see* Davis R. Dewey, *State Banking Before the Civil War*, *reprinted in* NATIONAL MONETARY COMMISSION REPORT 162-63, S. DOC. No. 581, 61st Cong., 2d Sess. (1910), and for buying notes from brokers, ALBERT O. GREEF, THE

(continued...)

requirements.[33] Each of these transactions allowed banks to impose lending charges in addition to, or instead of, periodic time-based payments.

The practice of discounts was particularly widespread in the nineteenth century.[34] In fact, discounts and bills of exchange were so common that Congress explicitly provided in Section 85 that banks could receive "interest" in these transactions.[35] It is thus impossible to conclude that Congress intended that "interest" would include only time-based periodic percentage charges.

Indeed, Congress made its intention to cover all loan charges under Section 85 even clearer in its treatment of exchange fees: In the mid-nineteenth century, banks often exacted profits from bills of exchange by charging, in addition to a discount or percentage-based interest rate,

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[32](...continued)
COMMERCIAL PAPER HOUSE IN THE UNITED STATES 14-15 (1938). A considerable body of law developed as to whether broker fees and other similar commissions could be considered usurious. *See* Annotation, *Usury: Expenses or Charges in Forms of Commissions to Agents, Brokers, or Like Intermediaries Incident to Loan of Money*, 52 A.L.R. 2d 703 (1957) (collecting cases from 19th and 20th centuries).

[33] Banks often required borrowers to keep a portion of funds lent — called a "compensating balance" — in the bank, thus allowing the bank to receive a higher effective rate of interest on the money that actually left the bank. JAMES, *supra*, at 84; GREEF, *supra*, at 15 n.35 (*quoting* CONDY RAGUET, A TREATISE ON CURRENCY AND BANKING 105 (1840)).

[34] *See* JAMES, *supra*, at 55-56; J.S. GIBBONS, THE BANKS OF NEW YORK, THEIR DEALERS, THE CLEARING HOUSE, AND THE PANIC OF 1857, at 236-37 (1859) (1857 bank statement shows "bills discounted" as almost 60% of assets and over 18 times the amount of "loans").

[35] "[E]very association may take, receive, reserve, and charge on any loan or *discount* made, or upon any note, *bill of exchange*, or other evidences of debt, interest at the rate allowed by the laws of the state . . . where the bank is located . . . ." (Emphasis added.)

exchange fees that were greater than the difference in currency value between the two locations involved in the transaction.[36] The practice had received the attention of numerous state governments and banking regulators prior to enactment of the Act. Dewey, *supra*, at 168-76. Section 85 specifically addressed this problem: an exchange fee "at not more than the current rate of exchange for sight drafts in addition to the interest, shall not be considered as taking or receiving a greater rate of interest." Congress thus specifically recognized that exchange fees in excess of the "current rate of exchange for sight drafts" (*i.e.*, the market rate) were within the definition of "interest" in Section 85.[37]

These provisions of Section 85 confirm that Congress intended to use the term "interest" in accordance with its generally accepted meaning in 1864 and to apply it to a wide variety of lending charges other than periodic time-based percentage payments. There is no principled reason for excluding late fees from that usage.

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[36] For example, if the current rate of exchange between Connecticut and New York was ¼%, a bank might charge the customer as high as 3%. *See* Dewey, *supra*, at 167-68.

[37] In debating the National Currency Act, which contained a similar provision, Senator Sherman contended that "bankers can make a reasonable profit under this bill I have no doubt" because, in part, "[t]hey have the benefit of exchange; not the rates of exchange formerly paid, but that incidental exchange which every bank draws in charges in drawing a draft, probably a quarter or a half of one percent." CONG. GLOBE, 37th Cong., 3d Sess. 875 (1863) (remarks of Sen. Sherman). This clear statement of Congressional intent was later embodied in Section 85: although the small exchange fees reflecting the bank's cost of exchanging currency would be exempted from Section 85, larger fees imposed in connection with bills of exchange *would be* included in the definition of "interest."

D. The Broad, Historical Definition of Interest Is Consistent with Congress's Objective in Enacting the National Bank Act.

The broad, historical definition of interest, as including all lending charges, is consistent with, and indeed compelled by, Congress's objectives in enacting the Act. Absent such a provision governing lending, interstate commerce could be seriously impeded because each state could impose its own separate limits on late fees and other charges on every national bank, thus greatly burdening the process of interstate lending, and national banks would lack the flexibility to deal with a wide variety of forms of credit extensions and changing financial and economic circumstances.

III. Consistent Construction of the National Bank Act

In the years immediately after passage of the Act, the courts interpreted its scope and effect broadly in order to assure that, as Congress intended, the newly established federal instrumentalities were protected from state interference. As this Court explained only ten years after passage of the Act, "National banks have been National favorites. They were established for the purpose, in part, of providing a currency for the whole country, and in part to create a market for the loans of the General government." *Tiffany* v. *National Bank*, 85 U.S. (18 Wall.) 409, 413 (1874). In order to effectuate that purpose, the *Tiffany* decision bestowed upon national banks the status of "most favored lender," a doctrine subsequently adopted by the OCC. *See Marquette Nat'l Bank* v. *First of Omaha Serv. Corp.*, 439 U.S. 299, 314 n.26 (1978).

The following year, this Court again confirmed that Sections 85 and 86 should "be liberally construed to effect the object which Congress had in view in enacting [them]." *Farmers' & Mechanics' Nat'l Bank* v. *Dearing*, 91 U.S. 29, 35 (1875). The Court concluded that these sections "cover the entire subject" of national bank lending and that "the

power to supplement [them] by State legislation is conferred neither expressly nor by implication." *Id.* at 32, 35. In words of equal force here, the Court in *Dearing* also reaffirmed the goal of uniformity under the Act by rejecting the defendant's proposed interpretation of Sections 85 and 86, which would have led to divergent penalties for violating interest rate ceilings in different states:

> A purpose to produce or permit such a state of things ought not to be imputed to Congress, unless the circumstances are so cogent as to render that result inevitable.

Id. at 33.

This approach to construing Section 85 continued in subsequent decisions. In *Citizens National Bank* v. *Donnell*, 195 U.S. 369 (1904), this Court applied Section 85 to cover late charges (specifically, monthly charges on an overdrawn account), thus recognizing the broad definition of "interest" intended by Congress. Other federal and state court decisions — often without even considering the possibility that interest could be more narrowly defined — have consistently so applied Section 85 for over a hundred years. Most relevant here, they have consistently held that Section 85 covers all lending charges received by a national bank whether or not there was a time element.[38]

[38] These charges have included bonuses and commissions, *Cronkleton* v. *Hall*, 66 F.2d 384 (8th Cir.), *cert. denied*, 290 U.S. 685 (1933); *Baker* v. *Lynchburg Nat'l Bank*, 91 S.E. 157 (Va. 1917); credit card cash advance charges, *Fisher* v. *First Nat'l Bank*, 548 F.2d 255 (8th Cir. 1977); charges for mortgage taxes and recording fees, *Panos* v. *Smith*, 116 F.2d 445 (6th Cir. 1940); *Schumacher* v. *Lawrence*, 108 F.2d 576 (6th Cir. 1940); compensating balance requirements, *American Timber & Trading Co.* v. *First Nat'l Bank*, 690 F.2d 781 (9th Cir. 1982); *McAdoo* v. *Union Nat'l Bank*, 535 F.2d 1050 (8th Cir. 1976); and brokerage fees, *In re Gerber's Estate*, 9 A.2d 438 (Pa. 1939).

Construing Section 85 in recent years, this Court has reaffirmed that the primary purpose of the Act was to foster interstate lending free of state law interference. Thus, in *Marquette*, this Court unanimously held that Section 85 preempts the application of any state laws limiting credit card lending rates to national banks' interstate credit card accounts because it is "implausible to conclude . . . that Congress meant . . . to exempt interstate loans from the reach of [Section 85]." 439 U.S. at 318. Indeed, as Senator Johnson stated during debates on the Act:

> These [national] banks will, of course, have very extensive loan transactions all over the country. They are organized for that purpose, and they will be sure to carry it out to the whole extent of the power, if they can do it with anything like safety to themselves.[39]

This broad concept of interest for purposes of Section 85 has been repeatedly accepted by the OCC, which has exclusive supervisory responsibility for national banks. *See* 12 U.S.C. §§ 21 *et seq.* For years, the OCC has interpreted Section 85 broadly to include all charges, in furtherance of Congress's clear purpose to protect national bank lending from state regulation.[40]

[39] CONG. GLOBE, 38th Cong., 1st Sess. 2021 (1864) (remarks of Sen. Johnson).

[40] *See, e.g.*, 61 Fed. Reg. 4849, 4869 (1996) (to be effective on April 1, 1996 and codified at 12 C.F.R. § 7.4001); Letter from Robert B. Serino, OCC Deputy Chief Counsel (Policy) 2 (Aug. 11, 1988), *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,676, at 78,064 (OCC Interpretive Letter No. 452); Letter from William P. Bowden, Jr., OCC Chief Counsel, 1992 WL 136390 (OCC) (Feb. 4, 1992); Letter from Richard V. Fitzgerald, Director, OCC Legal Advisory Servs. Div. 3-4 (Nov. 24, 1980).

Conclusion

For the reasons stated, the judgment of the Supreme Court of California should be affirmed.

Respectfully submitted,

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